S. HRG. 99-201 PT. II

Addendum
BROKERED DEPOSITS

HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

ON

OVERSIGHT HEARING ON THE BROKERED DEPOSITS MARKET CONCERNING THE BENEFITS, AND ABUSES TO THE ECONOMY, THE CONSUMER, AND THE FEDERAL INSURANCE SYSTEM

PART II

JUNE 5, 1985

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ADDENDUM

This addendum is being published due to the inadvertent omission of the committee's written questions and responses from:

Edwin J. Gray, Chairman, Federal Home Loan Bank Board.

The committee regrets this error.

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BROKERED DEPOSITS

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Federal Home Loan Bank Board

EDWIN J. GRAY
CHAIRMAN

1700 G Street, N.W.
Washington, D.C. 20552
Federal Home Loan Bank System
Federal Home Loan Mortgage Corporation
Federal Savings and Loan Insurance Corporation

October 22, 1985

Honorable Slade Gorton, Chairman
Subcommittee on Financial Institutions
and Consumer Affairs of the Committee
on Banking, Housing, and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Gorton:

In your June 14, 1985, letter to me you requested that I respond in writing to a number of further questions in connection with my appearance before the Subcommittee to testify on the subject of brokered deposits. I am enclosing for the record written answers to the questions you posed in your June 14th letter.

Additionally, in response to a telephone call to staff from Ed Malan, editor of the Senate Banking Committee hearings, regarding page 43 of the transcript of the June 5, 1985, hearing, the Board has already submitted proposed legislation dealing with the problem of brokered deposits, which is in Title I of S. 759.

Please let me know if I can be of further assistance.

Sincerely,

Edwin J. Gray

Enclosure

Question. Can you say how much is outstanding in brokered deposits at FSLIC insured institutions? Of this, how much is insured? Of the insured amount, how much is in troubled institutions (CAMEL rated 3, 4, or 5)? Of this amount, how much is short term and how much is long term? Finally, how many FSLIC insured institutions hold brokered deposits, and of these, in how many do brokered deposits exceed 5% of total assets?

Answer. FSLIC-insured institutions held $43.0 billion in brokered deposits on December 31, 1984, representing 5.5% of total deposits at these institutions. About 81% of all brokered deposit balances at FSLIC-insured institutions were probably covered by FSLIC insurance at year-end 1984, and about 63.5% of these balances were in "troubled" institutions with CAMEL-type ratings 3, 4, and 5. The Bank Board does not regularly collect data on the term to maturity of broker-originated deposits. The only time such information was obtained was in a special sample survey covering December 31, 1983. This survey indicated that as of that date 58% of all broker-originated deposits in accounts with balances of less than $100,000 at FSLIC-insured institutions had a remaining term to maturity of one year or less. Only 24%, or 739, of the 3,135 FSLIC-insured institutions held brokered deposits on December 31, 1984. Brokered deposits accounted for more than 5% of total deposits in 350 institutions, or 47% of those with any brokered deposits.

Question 1. A number of observers have suggested that aggressive examination and supervision, coupled with a prohibition on the garnering of insured brokered funds by troubled institutions, is sufficient to solve the problem. Why is this not so in your view?

Answer. The Bank Board vigorously enforces all statutes and regulations within its jurisdiction, including the final rule on brokered deposits adopted January 31, 1985, which attempts to limit the access of institutions with low net worth to brokered deposits. As the Board has noted in the past, however, these approaches focus only on the access of particularly vulnerable thrifts to brokered funds. They will not prevent abuses by institutions that were not of supervisory concern prior to their last examination. In addition, thrifts in desperate circumstances may be willing to violate regulations and acquire brokered funds to stave off failure. The ultimate loss borne by the FSLIC to resolve such cases will be significant. Finally, direct supervisory efforts are often unsatisfactory in detecting brokered funds abuses because substantial brokered deposits may be acquired and invested in a very short period. In short, examination and supervision are, by their very nature, after-the-fact and after-the-loss.

Question 2. What is your evaluation of the two alternative proposals for dealing with brokered deposits contained in this year's H.R. 15 and H.R. 107?

Answer. Although a step in the right direction, neither bill represents a fully effective approach to the brokered deposits problem. H.R. 15 limits the amount of all brokered deposits an institution may accept and provides for fines, but it has no reporting requirement and places no limit on the insurance of brokered deposits. H.R. 107 limits insurance coverage to $100,000 per broker per depositor in any four-year period, but it limits only the amount of short-term brokered deposits an institution may accept. It provides for no fines, but it does require reports from both institutions and deposit brokers.

What the FSLIC really needs is legislative confirmation of its ability to classify insurance of accounts as a means of limiting the amount of federal deposit insurance coverage of brokered deposits. So long as brokered deposits placed in institutions are fully insured despite the fact that they may be there in violation of the law, deposit brokers and troubled institutions will continue to gamble with federal deposit insurance funds. What the FSLIC needs from the Congress is the clear ability to up the ante.

Question 3. Mr. Falzon, in his testimony, maintained that brokered deposits placed on behalf of individuals have "not been associated with any of the problems the FDIC and the (FHLBB) have attributed to deposit brokerage." If you have evidence to the contrary, would you submit it for the record, please?

Answer. The Bank Board does not maintain separate records concerning the use of brokered deposits placed on behalf of individuals. However, the Securities Industry Association ("SIA"), a trade association of brokerage firms, has represented that its members place insured deposits primarily on behalf of individuals. In two specific instances, SIA members placed large volumes of insured deposits in troubled institutions. Merrill Lynch placed over $75 million in deposits at First National Bank of Midland, Texas, before it failed. Shearson/American Express placed $25 million in brokered deposits in Home Federal Savings and Loan Association of Puerto Rico, virtually doubling its size. The Shearson broker also participated in the placement of those funds into poor investments, which contributed to the failure of the institution.

Moreover, in testimony on July 16, 1985, before the Subcommittee on General Oversight and Investigations of the House Committee on Banking, Finance and Urban Affairs, William Isaac, Chairman of the FDIC, listed the 25 largest suppliers of insured brokered deposits to troubled FDIC-insured banks and thrifts. The three largest suppliers of such funds are SIA members, which, as I have mentioned, place insured deposits largely on behalf of individuals. Merrill Lynch supplied over $770 million to troubled FDIC-insured institutions, Dean Witter Reynolds, Inc., supplied $447 million, and Prudential Bache Securities, Inc., supplied over $130 million.

Question 4. In your testimony you referred to the large amounts of brokered deposits held by the failed Empire S&L and San Marino S&L. In each case, how much of these deposits were insured, and how much was short term v. long term?

Answer. At Empire, over 97% of the $305 million in total deposits was insured. Brokered deposits accounted for 66% of total deposits. At San Marino, 99% of the $245 million in total deposits was insured. When San Marino was closed brokered deposits accounted for 52% of total deposits, a percentage which had been greatly reduced by the placement of a conservator at the institution ten months prior to closing. The small amounts of uninsured funds at both institutions represented, with few exceptions, accrued interest on jumbo accounts which exceeded the $100,000 limit.

Standard reports from insurance settlement cases provide detailed information regarding term and ownership characteristics only for jumbo certificate accounts. Maturity length data is readily available for all jumbo certificates, but not for brokered jumbo certificates. Our experience has been, however, that brokered deposits are almost always in the form of jumbo accounts.

With these caveats, however, I can report that at Empire jumbo deposits accounted for 95% of total deposits. Of these jumbo deposits, 94% were short-term (7% held by individuals; 87% held by corporations), and 6% were long-term (all held by corporations). At San Marino jumbo deposits accounted for 64% of total deposits. Of these jumbo deposits, 22% were short-term (all held by individuals), and 78% were long-term (4% held by individuals; 74% held by corporations).

Question 5. On page 13 of your testimony you stated that the FSLIC currently has ". . . the ability to set percentage limits on the share of insured brokered funds institutions (subject to its regulation) can accept." First, what is the statutory authority for this; and second, if this is so, why do you need additional legislation?

Answer. The statutory authority of the FSLIC to set these limits lies in its responsibility, granted in the National Housing Act, to require the institutions it insures to operate in a safe and sound manner. More specifically, the Board's authority is found in sections 402, 403, and 407 of the National Housing Act (12 U.S.C. §§ 1725, 1726, 1730). The FSLIC needs additional clarifying legislation because only the classification of accounts for insurance purposes will deprive deposit brokers and troubled, often desperate institutions of the ability to gamble with federal deposit insurance funds.

Question 6. Based on your experience with insured deposits in failed institutions, to what degree are short term deposits owned by individuals; and to what degree are long term deposits owned by institutions?

Answer. An analysis of the past twenty insurance settlement cases (1982 to present) shows, with only a few exceptions, a high proportion of corporately held, short-term jumbo accounts. Information which associates term and ownership characteristics is available for fifteen of the twenty cases. A summary of these follows. Please note that the figures shown are as of the date of default for failed institutions. The appointment of a conservator for several institutions greatly reduced the proportion of jumbo certificates in the months prior to closing. Data for the remaining five cases shows high percentages of short-term certificates, as well as high percentages of corporately held certificates, although exact figures are not available as to how many certificates are both short-term and corporately held. Please refer to my remarks on data constraints in my answer to Questions 3 and 4 above.

		% OF TOTAL DEPOSIT DOLLARS			
	% JUMBO	LONG TERM (More than 1 yr.)		SHORT TERM (1 yr. or less)	
CASE	CERTIF.	CORPORATE	INDIVIDUAL	CORPORATE	INDIVIDUAL
Valley First FS&LA	56	5	0	51	0
Cleveland Community	69	0	0	68	0
Union S&L	8	0	0	8	0
Empire S&L	66	6	0	87	7
American S&L	80	5	0	56	3
Savannah S&L	73	5	0	62	5
Knox FS&LA	21	0	0	17	4
East TN S&LA	10	0	0	9	1
American S&LA	16	0	1	6	9
John Sevier S&LA	75	22	0	52	1
San Marino S&LA	21	2	0	10	9
Western Community	69	0	0	55	14
State S&LA (Hawaii Div)	8	4	0	4	4
State S&LA (Utah Div)	78	3	3	10	6
Community FS&LA	64	63	1	0	0
Magnolia FS&LA	47	0	0	47	0

I am also supplying tables showing, as a percent of total deposits at FSLIC-insured institutions that have failed since April 1985, the highest-ever level of brokered deposits and the level of brokered deposits at the time of receivership.

Brokered Deposit Report
Receiverships, MCPs, Passthroughs and Liquidations
REGION I
(000s Omitted)

District/ Docket No.	(Since 4/85) Institution Name	#1 Total Deposits at Time of Highest Level of Brokered Deposits	%Brokered Deposits to Total #1	#2 Total Deposits at Time of Receivership	% Brokered Deposits to Total #2
02 1726	Flushing FS&LA Flushing, NY	$458,874 (Dec. '84)	14.39%	$520,123 (Jun '85)	4.68%
05 7328	Magnolia FS&LA Knoxville, TN	None.	0.00%	$ 3,655 (Jun '85)	0.00%
05 6733	Community FS&LA Nashville, TN	$ 18,798 (Mar '85)	55.30%	$ 16,300 (Jun '85)	50.20%

Brokered Deposit Report
Receiverships, MCPs, Passthroughs and Liquidations
REGION II
(000s Omitted)

District/ Docket No.	(Since 4/85) Institution Name	#1 Total Deposits at Time of Highest Level of Brokered Deposits	%Brokered Deposits to Total #1	#2 Total Deposits at Time of Receivership	% Brokered Deposits to Total #2
11 6186	Central S&LA (2) San Diego, CA	$1,613,636 (June '83)	4.40%	$1,631,579 (May '85)	3.80%
11 7501	Centennial S&LA Durango, CA	$218,834 (Mar. '84)	66.90%	$391,803 (Aug. '85)	6.10%
11 3630	Butterfield S&LA Temecula, CA	$504,674 (Mar. '84)	81.30%	$768,750 (Aug. '85)	3.20%
11 8000	Golden Pacific S&LA Windsor, CA	$41,221 (Aug. '85)	100.00% (1)	$41,221 (Aug. '85)	100.00% (1)
11 2268	Eureka FS&LA (2) San Carlos, CA	$1,134,194 (Mar. '84)	15.50%	$1,388,235 (June '85)	1.70%
11 7419	Presido S&LA Porterville, CA	$135,360 (June '84)	88.80%	$231,851 (Aug. '85)	56.20%
11 1693	Bell S&LA San Mateo, CA	$850,688 (Oct. '83)	50.90%	$1,164,557 (July '85)	7.90%
11 4061	Beverly Hills Savings, a FS&LA Beverly Hills, CA	$2,515,059 (Jan. '84)	42.50%	$2,077,889 (Apr. '85)	39.80%
11 1971	Southern California S&LA, a FS&LA Beverly Hills, CA	$1,129,482 (Mar. '84)	25.10%	$317,857 (June '85)	2.80%
07 6110	Glen Ellyn S&LA Glen Ellyn, CA	$79,988 (July '84)	19.31%	$96,654 (Aug. '85)	3.29%
07 2831	First FS&LA of Freeport* Freeport, IL	N/A	0.00%	$33,968 (May '85)	0.00

* No Brokered Deposits Reported

(1) OES Estimate
(2) In MCP. Did not go through receivership

Brokered Deposit Report
Receiverships, MCPs, Passthroughs and Liquidations
REGION III
(000s Omitted)

District/ Docket No.	(Since 4/85) Institution Name	#1 Total Deposits at Time of Highest Level of Brokered Deposits	%Brokered Deposits to Total #1	#2 Total Deposits at Time of Receivership	% Brokered Deposits to Total #2
04 7737	Sunrise S&LA* Boynton Beach, FL	NA	0%	$1,496,482 (June '85)	0%
04 7305	Family FS&LA Springfield, VA	$65,364 (June '83)	41.37%	$ 69,162 (Aug. '85)	0%
04 5808	Northern Virginia S&LA, A FA* Arlington, VA	NA	0%	$ 234,147 (Apr. '85)	0%
12 7793	Montana FSB Kalispell, MT	$29,258 (June '83)	50.28%	$ 30,491 (July '85)	20.01%
12 0937	Westside FS&LA* Seattle, WA	NA	0%	$ 314,517 (July '85)	0%

*No Brokered Deposits Reported.

Brokered Deposit Report
Receiverships, MCPs, Passthroughs and Liquidations
REGION IV
(000s Omitted)

District/ Docket No.	(Since 4/85) Institution Name	#1 Total Deposits at Time of Highest Level of Brokered Deposits	%Brokered Deposits to Total #1	#2 Total Deposits at Time of Receivership	% Brokered Deposits to Total #2
09 3597	Bell SA Temple, TX	$298,468 (Sept. '84)	67.64%	$272,540 (Aug. '85)	24.58%
09 5730	Heights SA* Houston, TX	NA	0.00%	$409,568 (Sept. '85)	0.00%
09 7522	Citizens S&LA Batesville, MS	$21,010 (June '83)	36.67%	$13,217 (June '85)	0.00%
09 7760	Northlake FS&LA Covington, LA	$104,796 (Mar. '84)	64.71%	$119,076 (June '85)	5.04%
09 7831	Alliance FS&LA Kenner, LA	$115,812 (June '84)	39.35%	$113,999 (Aug. '85)	8.87%
10 7628	Century SA of Kansas Shawnee Mission, KS	$52,487 (Dec. '83)	4.95%	$44,661 (June '85)	4.03%
10 7590	Sierra S&LA Denver, CO	$81,442 (June '85)	72.73%	$84,123 (Aug. '85)	72.30%

* No Brokered Deposits Reported.